Supreme Court, U. S.
FILED
AUG 31 1977
MICHAEL RODAK, JR., CLERK

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1976

No. 76-1114

THE PEOPLE OF THE STATE OF CALIFORNIA and the PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA, *Petitioners,*

vs.

SOUTHLAND ROYALTY COMPANY, et al., TEXACO INC., EXXON CORPORATION and MOBIL OIL CORPORATION, *Respondents.*

No. 76-1133

EL PASO NATURAL GAS COMPANY, *Petitioner,*

vs.

SOUTHLAND ROYALTY COMPANY, et al., TEXACO INC., EXXON CORPORATION and MOBIL OIL CORPORATION, *Respondents.*

No. 76-1587

FEDERAL POWER COMMISSION, *Petitioner,*

vs.

SOUTHLAND ROYALTY COMPANY, et al., *Respondents.*

On Writs of Certiorari to the United States Court of Appeals for the Fifth Circuit

BRIEF OF PETITIONERS THE PEOPLE OF THE STATE OF CALIFORNIA AND THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

JANICE E. KERR,
J. CALVIN SIMPSON,
RANDOLPH W. DEUTSCH,
5066 State Building,
San Francisco, California 94102,
Attorneys for Petitioners the People of the State of California and the Public Utilities Commission of the State of California.

Dated: August 31, 1977.

PERNAU-WALSH PRINTING CO. - 562 MISSION STREET - SAN FRANCISCO, CA 94105

Subject Index

	Page
Opinions below	2
Jurisdiction	2
Question presented	2
Statutory provisions involved	3
Statement of case	3
Summary of argument	6
Argument	9
I. The commission's order in this matter complies with the statutory requirements and applicable case law	11
II. The purposes to be served by the Natural Gas Act require a reversal of the lower court's decision	24
Conclusion	31

Table of Authorities Cited

Cases

Atlantic Refining Company v. Public Service Commission of New York, 360 U.S. 378 (1959) 11, 12, 26

California v. Lo-Vaca Gathering Company, 379 U.S. 366 (1965) 9, 16, 17

Federal Power Commission v. Hope Natural Gas Company, 320 U.S. 591 (1944) 21, 22, 25, 29

Federal Power Commission v. Transcontinental Gas Pipe Line Corporation, 365 U.S. 1 (1961) 22, 23, 29

Federal Power Commission v. Hunt, 376 U.S. 515 (1964) 30

Federal Power Commission v. Louisiana Power and Light Company, 406 U.S. 621 (1972) 23, 25, 29

Federal Power Commission v. Moss, 424 U.S. 494 (1976) 28

Gulf Oil Corporation v. Southland Royalty Company, 496 S.W.2d 547 (Tex. 1973) 4

Mitchell Energy Corporation v. Federal Power Commission, 533 F.2d 258 (5th Cir. 1976) 17, 18

Mobil Oil Corporation v. Federal Power Commission, 463 F.2d 256 (D.C. Cir. 1971), cert. denied, 406 U.S. 976 (1972) 19, 20, 29

Panhandle Eastern Pipe Line Company v. Public Service Commission of Indiana, et al., 332 U.S. 507 (1947) 23

Phillips Petroleum Company v. Wisconsin, 347 U.S. 672 (1954) 22

Southland Royalty Company v. Federal Power Commission, 543 F.2d 1134 (5th Cir. 1976) 6

Sun Oil Company v. Federal Power Commission, 364 U.S. 170 (1960) 14, 28

Sunray Mid-Continent Oil Company v. Federal Power Commission, 364 U.S. 137 (1960) ..13, 14, 15, 16, 18, 20, 26, 27, 29, 31

United Gas Improvement Company v. Continental Oil Company, 381 U.S. 392 (1965) 10, 28, 29

United Gas Pipe Line Company v. Federal Power Commission, 385 U.S. 83 (1966) 10, 18, 28

Federal Power Commission Cases

Page

El Paso Natural Gas Company, et al., Opinion No. 737, ___ F.P.C. ___, Docket Nos. CP 75-209, et al. (issued July 11, 1975) 2

El Paso Natural Gas Company, et al., Opinion No. 737-A ___ F.P.C. ___, Docket Nos. CP 75-209, et al. (issued September 3, 1975) 2

Northern Natural Gas Company v. John L. Crawford, ___ F.P.C. ___, Docket No. CS71-6 (issued September 29, 1976), appeal docketed sub nom. Harrison v. F.P.C., No. 76-4319, 5th Cir. December 13, 1976 31

Statutes

Interstate Commerce Act, Section 1(18) as added by the Transportation Act of 1920, 41 Stat. 477, 49 USC, Section 1(18) 14

Federal Communications Act, Section 214(a) as amended by the Act of March 6, 1943, 57 Stat. 11, 47 USC Section 214(a) 14

Natural Gas Act, 15 U.S.C. Section 717, et seq. (1938) 3

In the Supreme Court
OF THE
United States

OCTOBER TERM, 1976

No. 76-1114

THE PEOPLE OF THE STATE OF CALIFORNIA and the PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA, *Petitioners,*

vs.

SOUTHLAND ROYALTY COMPANY, et al., TEXACO INC., EXXON CORPORATION and MOBIL OIL CORPORATION, *Respondents.*

No. 76-1133

EL PASO NATURAL GAS COMPANY, *Petitioner,*

vs.

SOUTHLAND ROYALTY COMPANY, et al., TEXACO INC., EXXON CORPORATION and MOBIL OIL CORPORATION, *Respondents.*

No. 76-1587

FEDERAL POWER COMMISSION, *Petitioner,*

vs.

SOUTHLAND ROYALTY COMPANY, et al., *Respondents.*

On Writs of Certiorari to the United States Court of Appeals for the Fifth Circuit

BRIEF OF PETITIONERS THE PEOPLE OF THE STATE OF CALIFORNIA AND THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

OPINIONS BELOW

The opinion of the Court of Appeals is reported at 543 F.2d 1134. The Federal Power Commission's (Commission) Declaratory Opinion and Order on Termination of Long-Term Leases, Opinion No. 737, in the consolidated proceeding styled *El Paso Natural Gas Company,* Docket No. CP75-209, and *Texaco, Inc.,* Docket No. CI75-594, issued July 11, 1975, is not yet reported and is printed at Joint Appendix page 598. The Commission's Opinion and Order Denying Rehearing but Adopting Per Curiam, Opinion No. 737-A in Docket No. CP75-209 and CI75-594, issued September 3, 1975, is not yet reported and is printed at Joint Appendix page 708.

JURISDICTION

The judgment of the Court of Appeals was entered on December 13, 1976. A petition for a writ of certiorari to the United States Court of Appeals for the Fifth Circuit was filed on February 11, 1977. On June 27, 1977, this Court granted the petition for a writ of certiorari. The jurisdiction of this Court is invoked under 28 U.S.C. Sec. 1254(1) and Sec. 19(b) of the Natural Gas Act, 15 U.S.C. Sec. 717r(b).

QUESTION PRESENTED

Whether the Natural Gas Act, Section 7(b) requires reversionary mineral interest owners of certain gas producing lands to obtain abandonment authorization from the Commission before they can terminate sales of a continuing flow of natural gas for resale in interstate commerce when the initial dedication of the gas was made by leaseholders of 50-year fixed-term leases that have expired.

STATUTORY PROVISIONS INVOLVED

Involved here are provisions of the Natural Gas Act, 15 U.S.C. Sections 717-717w. Resolution of the issues presented turns especially upon Sections 1(b) and 7(b), (c), and (e), 15 U.S.C. Section 717(b) and 717f(b), (c) and (e). These provisions are set forth in Appendix A.

STATEMENT OF CASE

This case commenced before the Commission in two consolidated proceedings involving the issue of the necessity for abandonment authorization pursuant to Section 7(b) of the Natural Gas Act as a result of the expiration of two 50-year fixed-term oil and gas leases. On July 14, 1925, Gulf Oil Corporation (Gulf), then Gulf Production Company, entered into an oil and gas lease with W. N. Waddell (Waddell Lease) under which Gulf obtained the exclusive right to explore for, produce and market all oil and gas from 45,771 acres of land in Crane County, Texas for a 50-year period. On January 26, 1951 and March 1, 1972, respectively, Gulf entered into two surplus

residue gas purchase contracts with El Paso Natural Gas Company (El Paso) whereunder Gulf sold to El Paso at the outlet of Gulf's Waddell Gasoline Plant natural gas produced from the Waddell Lease. Gulf received a certificate of public convenience and necessity from the Commission authorizing the sale of such gas for resale in interstate commerce to El Paso. El Paso, in turn, transports such gas in interstate commerce through its interstate pipeline system for distribution and resale in the states of Texas, New Mexico, Arizona, Nevada and California. Upon expiration of the Waddell Lease on July 14, 1975, the reversionary mineral interest owners[1] obtained under Texas law unconditional title to the mineral estate underlying the Waddell Lease. *Gulf Oil Corp. v. Southland Royalty Co.*, 496 S.W.2d 547 (Tex. 1973). Shortly prior to the termination of the Waddell Lease, Southland Royalty Company, under claim of its reversionary interest, contracted with an intrastate pipeline, Intratex Gas Company, effective as of the time of termination of the lease, to sell the gas which Gulf had not produced from the same formations from which gas previously had been produced, sold and delivered to El Paso for resale in interstate commerce.

On August 7, 1925, Gulf entered into a similar 50-year fixed-term oil and gas lease with Goldsmith

[1]Southland Royalty Company has ownership of approximately 47% of the acreage involved; trustees under the will of Warren Wright have 25.7%; Exxon Corporation (Exxon) has 14%; and Mobil Oil Corporation (Mobil) and more than 100 others own lesser shares.

and others (Goldsmith Lease) under which Gulf obtained exclusive mineral rights to some 19,840 acres in Ector County, Texas. Gulf sold the gas attributable to gas reserves covered by the Goldsmith Lease to Phillips Petroleum Company (Phillips) pursuant to a certificate of public convenience and necessity issued by the Commission. Phillips sold such gas to El Paso at the outlet of Phillips' Goldsmith Plant pursuant to certificates of public convenience and necessity granted by the Commission, and El Paso, in turn, transports it through its interstate gas transmission facilities for subsequent resale in interstate commerce. The Goldsmith Lease expired on August 7, 1975 and title to the mineral estate reverted to the reversionary mineral interest owners.[2]

On January 20, 1975, El Paso petitioned the Commission in Docket No. CP75-209 for a declaratory order determining whether the Waddell Lease reversionary mineral interest owners could, when the Waddell Lease expired, cease gas deliveries to El Paso and sell the gas for resale in intrastate commerce without prior abandonment authorization pursuant to Section 7(b) of the Natural Gas Act. On April 8, 1975, Texaco petitioned the Commission in Docket No. CI75-594 for a similar determination regarding gas produced from reserves covered by the Goldsmith Lease. The Commission consolidated

[2]Texaco Inc. (Texaco) owns approximately 25% of the acreage formerly covered by the Goldsmith Lease. Southland Royalty Company and several other parties own fractional parts of the remaining acreage.

Docket Nos. CP75-209 and CI75-594. No factual issues being in dispute, no evidentiary hearings were held.

The Commission issued Opinion Nos. 737 and 737-A on July 11, 1975 and September 3, 1975, respectively, wherein it determined that the reversionary mineral interest owners were subject to the dedications made by leaseholder Gulf for the sale of gas for resale in interstate commerce to El Paso and that, upon termination of the leases, they could not divert the gas into intrastate commerce without first obtaining abandonment approval under Section 7(b) of the Natural Gas Act.

Petitions for review of Opinion Nos. 737 and 737-A were filed by reversioners Southland Royalty Company, Texaco, Exxon and Mobil in the United States Court of Appeals for the Fifth Circuit.[3] The Court of Appeals, in *Southland Royalty Co. v. Federal Power Commission,* 543 F.2d 1134 (5th Cir. 1976), reversed the decisions of the Commission and held that under applicable Texas law a lessee did not have "the right to encumber or restrict the reversionary estate" and, therefore, gas attributable to the reversioners' interests was not dedicated to interstate commerce.

SUMMARY OF ARGUMENT

This Court, in a line of cases involving Section 7(b) of the Natural Gas Act, has consistently given

[3]Hereinafter these reversionary mineral interest owners, respondents in this Court, are referred to as Southland Royalty Company.

the broadest interpretation to that section holding that once gas is dedicated to interstate commerce there can be no withdrawal of that supply from continued interstate movement without Commission approval. The Commission has been required to maintain strong control over ingress to and egress from the interstate gas market using the public interest as a standard. This Court has found the Commission to be in error for failing to review the price of gas in an application to serve the interstate market where private parties had agreed on the price and refused to submit it to the Commission to consider whether the price was in the public interest. A Commission issued certificate of unlimited duration was upheld against the protest of a producer requesting a certificate limited to a contract of sale. The Court supported the Commission in ordering a pipeline to continue the service dedicated by its predecessor after the termination of a sales contract. The Commission was overruled when it gave dispositive weight to private agreements in an abandonment proceeding.

In reviewing the requirement to seek abandonment authorization, this Court has recognized that the Natural Gas Act relates to the flow of gas in interstate commerce. It has held that gas flowing in a commingled stream both intrastate and interstate requires Commission certification. Federal jurisdiction follows the actual flow of gas, not the technicalities of legal agreements. Further the Court has stated that natural gas *service* involves the movement of gas in interstate commerce, while the initial gas sales contract is but the commencement of that service.

This Court's rationale has been made abundantly clear. The heart of the Natural Gas Act is found in those provisions requiring initially that any proposed service, sale, operation, construction, extension, or acquisition will be required by the present or future public convenience and necessity, that rates and charges will be just and reasonable, and that once gas is dedicated there can be no withdrawal of that supply without Commission approval. The primary aim of the Natural Gas Act is to give consumers a complete, permanent and effective bond of protection from excessive rates and charges. The Commission and this Court must look to the Congressional purpose of the Act as well as the practical, economic and public interest issues raised by any contention that the Natural Gas Act is inapplicable. In this regard, this Court has stated that the Act cannot be hamstrung by technical concepts of local law.

A court reviewing such a contention must look to the Natural Gas Act and the public interest for guidance, not private contracts or local law. Yet the lower court in this case violated this concept. It gave dispositive weight to the lease agreement involved and the local law governing it, distinguishing the strong precedents set by this Court. This effectively placed the consideration of the public interest in private hands, exactly the situation which must be guarded against. The question below is analyzed by the court in terms of property law *versus* regulatory powers. More properly, the analysis should have recognized that the Natural Gas Act imposes a regulatory requirement on the subject natural gas over and

above local law and lease agreements. The ownership rights in the subject gas, which remains undisturbed, cannot affect the service requirement which was undertaken by Gulf and which attached to the gas.

ARGUMENT

The jurisdiction of the Commission attaches to the transportation of natural gas in interstate commerce and to the sale for resale of natural gas in interstate commerce. Under Section 7(c) of the Natural Gas Act, no natural gas company can engage in such sale or transportation without a certificate of public convenience and necessity issued by the Commission. Section 7(b) of the Natural Gas Act precludes abandonment of that sale or transportation without Commission authorization. Section 7(b) requires a finding by the Commission that available supply is depleted or that "the present or future public convenience or necessity permits such abandonment." These provisions follow the normal regulatory structure created by Congress. It has long been recognized by Congress and this Court that a strong abandonment provision is required to make the Natural Gas Act viable. In fact, the abandonment procedure in the Natural Gas Act is the only legal avenue to withdraw the flow of natural gas from interstate commerce. This Court has held that once natural gas begins to flow in interstate commerce, it thereby becomes dedicated to interstate commerce. *(California v. Lo-Vaca Gathering Co.*, 379 U.S. 366, 369 (1965).) Further, it has been held that this flow of gas cannot be abandoned without Com-

mission authorization even if the contract for sale of that gas has expired. *(United Gas Pipe Line Company v. FPC,* 385 U.S. 83 (1966).)

Litigants before this Court have attempted through the use of various legal formulations to avoid this requirement. The issue in these cases, as in the instant one before the Court, is the extent to which natural gas reserves, once dedicated to interstate commerce, can be withdrawn from interstate commerce by means of transactions among private interested parties. This, in essence, becomes private control of the duration of the dedication of gas in interstate commerce and private control of the public interest.

This type of private arrangement was sucessfully supported in the court below. Southland Royalty Company argued that, under Texas law, a person holding a present interest in real property which is limited in duration cannot create an estate which will extend beyond the terms of his interest. Since Gulf, the leaseholder, never was possessed of rights in the gas under the leasehold lands which could survive the termination of its private 50-year lease, it never could create rights in a third person to that same gas.

Even though this Court has stated that a regulatory statute such as the Natural Gas Act would be hamstrung if it were tied to technical concepts of local law *(United Gas Improvement Co. v. Continental Oil Co.,* 381 U.S. 392, 400 (1965)) the court below chose to follow Texas law and ruled against the statutory mandate and line of cases supporting it. The Natural Gas Act as interpreted by this Court governs

the obligation to continue deliveries of natural gas in interstate commerce absent Section 7(b) abandonment authorization, once interstate gas service has been initiated. Local law cannot be permitted to frustrate that regulatory control.

Contrary to the view of the court below, the regulatory powers of the Natural Gas Act do not challenge property rights here. Rather they impose a regulatory requirement on the subject natural gas over and above local law and property rights.

I. THE COMMISSION'S ORDER IN THIS MATTER COMPLIES WITH THE STATUTORY REQUIREMENTS AND APPLICABLE CASE LAW.

This Court has through an extensive line of cases supported a very broad interpretation of the abandonment provision of the Natural Gas Act. Beginning with the *Catco* case *(Atlantic Refining Company v. Public Service Commission of New York,* 360 U.S. 378 (1959)) this Court has unequivocally enunciated its understanding of the Natural Gas Act. The *Catco* case, while involving different facts than the instant proceeding, revolved around essentially the same principle. In *Catco* the parties had agreed upon a price for gas prior to seeking a certificate of public convenience and necessity. The Commission granted the certificate without determining the fairness of the price. This decision was overturned because of the Commission's refusal to examine this vital aspect of the application. The thread that links the *Catco* case

to the proceeding before the Court and indeed runs through the entire line of cases on this subject is the issue of private arrangements *versus* regulatory control. The parties in the *Catco* case had established a price for the gas between themselves by private contract. In fact, the Natural Gas Act itself is built in the first instance on private contracts. However, the Natural Gas Act requires the Commission to determine whether these private agreements are in the public interest.

This Court in *Catco* stated in speaking of the Natural Gas Act:

> "The heart of the Act is found in those provisions requiring initially that any 'proposed service, sale, operation, construction, extension, or acquisition . . . will be required by the present or future public convenience and necessity.' §7(e), 15 USC §717f(e), and that all rates and charges 'made, demanded, or received' shall be 'just and reasonable' §4, 15 USC §717(c). The Act prohibits such movements unless and until the Commission issues a certificate of public convenience and necessity therefor, §7(c), 15 USC §717f(c). Section 7(e) vests in the Commission control over the conditions under which gas may be initially dedicated to interstate use. Moreover, once so dedicated there can be no withdrawal of that supply from continued interstate movement without Commission approval."[4]

The above language explains the basic operation of the Act. For without control over ingress and egress

[4] *Atlantic Refining Company v. Public Service Commission of New York, supra,* at 382, 388.

of the natural gas in interstate commerce there can be no effective protection of the public interest, the basic purpose of the Act.

This concept of regulatory control as it applies to abandonment of service was analyzed in depth in *Sunray Mid-Continent Oil Co. v. Federal Power Commission,* 364 U.S. 137 (1960). In this case the Court held that the Commission had authority to tender a certificate of public convenience and necessity without time limitation to an independent producer disregarding his request that the certificate be limited in time to the duration of the contract for the sale of gas which the producer had made. The practical result was that the expiration of a contract between a natural gas producer and an interstate pipeline company to sell gas in interstate commerce did not excuse the obligation to continue delivery of such gas until the requirements of Section 7(b) had been met. Similarly, the agreement contained in the leases in the instant case to limit Gulf's power to produce gas for a period of fifty years cannot be substituted for a proceeding under Section 7(b) to determine whether cessation of deliveries of gas is permitted by the public interest.

As recognized in the *Sunray* case, the Section 7(b) abandonment provision follows a common pattern in federal utility regulation.[5] This type of provision is also found in the Interstate Commerce Act and the

[5] *Sunray Mid-Continent Oil Co. v. Federal Power Commission,* 364 US 137, 141, 142.

Federal Communications Act.[6] Without this provision, private parties could withdraw service at will and avoid the regulatory scheme thereby thwarting the Commission's ability to protect the public. In the *Sunray* case the Court analyzed the motivation of the petitioners, the gas producers, in seeking to limit the Commission's authority to grant a certificate of public convenience and necessity to match the time limits set by their contract. The Court found that this would have the effect of allowing the parties before the Court to evaluate the interstate gas market on purely economic grounds when the subject contract expired thereby avoiding public interest considerations. But further, the significance of the petitioners' argument was that a ruling in favor of the petitioners would allow gas producers in the future to style sales contracts in such a fashion as to allow termination in any number of circumstances that they deemed unfavorable, untrammeled by Commission regulation.[7] This contention would effectively emasculate the Natural Gas Act. The abandonment provision would become little more than a means to enforce the terms of private contracts.

[6]Interstate Commerce Act, Section 1(18) as added by the Transportation Act of 1920, 41 Stat. 477, 49 USC Section 1(18); Federal Communications Act, Section 214(a) as amended by the Act of March 6, 1943, 57 Stat. 11, 47 USC Section 214(a).

[7]*Sunray Mid-Continent Oil Company v. Federal Power Commission, supra,* at 142. In a companion case, *Sun Oil Company v. Federal Power Commission,* 364 US 170 (1960) this Court again rejected the argument that the Commission must limit a certificate of public convenience and necessity to the period of a gas sales contract so that the contract governed the abandonment provision. The Court pointed out that the certificate that was issued authorized both the "sale" of natural gas and a "service" not limited to the underlying contract.

The duty to deliver gas after a sales contract expires is one imposed by the Act not by a contractual or private rights theory. In this regard, the Court in *Sunray* quickly set aside the petitioners' argument that a certificate of public convenience and necessity only authorized a specific sale. This Court recognized that under Section 7(e) of the Natural Gas Act, the Commission may issue a certificate authorizing the movement of gas in interstate commerce as a "service" and the sale of the gas is the commencement of that service.[8] Service as used in Section 7(b) of the Natural Gas Act means much more than the sale of gas in interstate commerce under a contract. It involves a consideration of the public interest. This includes the authority of the Commission to review rates, impose terms and conditions on the sale of the gas and order the continuation of the flow of gas in interstate commerce after contract expiration.

> "Further, the Power Commission has from an early date taken the view that there is a continuing obligation to perform 'service' imposed by the Act which outlasts the term of a seller's original contract of sale. As early as 1942 it held that an abandonment of service after the expiry of such a contract had to have Commission approval under §7(b) [Citation omitted]. . . . The ruling has been followed, see Panhandle Eastern Pipe Line Co., 11 FPC 167, 172, and we think this contemporaneous and consistent construction, pointing again to a distinction between the underlying 'service' to the public and the

[8]*Sunray Mid-Continent Oil Co. v. Federal Power Commission, supra,* at 149.

contractual means by which it is implemented, is to be afforded weight in the construction we make."[9]

In the instant case, the sole limitation imposed by the leases in question on Gulf's powers to sell gas was the 50-year duration of the leaseholds. Gulf had dedicated all of the reserves under those leaseholds to satisfy its obligation to sell gas in interstate commerce. The 50-year lease limitation does not alter the fact that all of the subject gas had been dedicated to interstate commerce. The service involved in selling that gas in interstate commerce must come within the ambit of Section 7(b).

The issue of regulation of the gas itself as well as the legal contractual arrangement in a specific instance have been further refined by this Court since the *Sunray* case.

The case of *California v. Lo-Vaca Gathering Co.*, 379 U.S. 366 (1965) considered this issue although in a slightly different context. Factually, the *Lo-Vaca Gathering Co.* case involved an order of the Commission declaring to be within its jurisdiction, as sales of natural gas in interstate commerce for resale, sales of natural gas in Texas, produced and delivered there, but flowing in a commingled stream with gas from other sources, a portion of which would be resold out of Texas. The authority of the Commission was challenged by the producer of the gas. This Court held that the fact that a substantial part of the gas would

[9] *Sunray-Mid-Continent Oil Co. v. Federal Power Commission, supra,* at 153, 154.

be resold in interstate commerce invoked federal jurisdiction at the outset over the entire transaction. This result was reached even though the sales were to be made under "restricted use" agreements explicitly limiting the gas in its use. This Court stated:

> "We said in Connecticut Co. v. Federal Power Commission, 324 U.S. 515, 529, 89 L.ed 1150, 1160, 65 S.Ct. 749, 'Federal jurisdiction was to follow the flow of electric energy, an engineering and scientific, rather than a legalistic or governmental, test.' And that is the test we have followed under both the Federal Power Act and the Natural Gas Act except as Congress itself has substituted a so-called legal standard for the technical one. (Citations omitted)."[10]

At first blush it could be argued here that this case is too remote factually from the case now before the Court to be helpful. However, the logical and necessary rationale of viewing the actual gas use and its effect under the Natural Gas Act as opposed to restricting the Commission to the legal agreement between the private parties was very much in evidence in the case. As Mr. Justice Douglas stated: "Were suppliers of gas and pipeline companies free to allocate by contract gas from a particular source to a particular use, havoc would be raised within the federal regulatory scheme . . ."[11]

The Circuit Court of Appeals for the Fifth Circuit itself ruled in *Mitchell Energy Corporation v. Federal Power Commission,* 533 F.2d 258 (1976) that the suc-

[10] *California v. Lo-Vaca Gathering Co., supra,* at 369.
[11] *Ibid.* at 369.

cessor in interest to a holder of a certificate dedicating all available natural gas in a certain field to interstate commerce was required to continue to deliver into interstate commerce all gas produced from that field. The successor producer argued that only the gas being produced from existing wells must be continued to be sold in interstate commerce. The original sales contract in this case had expired. However, since all the gas in the field had been dedicated to interstate commerce under the predecessor's certificate of public convenience and necessity, the court held that the entire field was dedicated and came under the Natural Gas Act.

The *Mitchell Energy Corporation* case relied on *United Gas Pipe Line Company v. Federal Power Commission* 385 U.S. 83 (1966) as authority as well as the *Sunray* case. This Court in *United Gas Pipe Line Company* upheld the decision of the Court of Appeals for the Fifth Circuit that the Commission had authority to order an interstate pipeline company after termination of a contract to purchase gas from a certain field to continue purchasing that gas at the producer's new rate approved by the Commission. The Court in analyzing the facts of that case again distinguished between "service" and "sales" of gas in interstate commerce.

The above cited cases present a comprehensive guideline to follow in judging a claim that a particular transaction concerning natural gas sold or transported in interstate commerce is not governed by Section 7(b). Case after case have given this pro-

vision of the Natural Gas Act the broadest interpretation and support.

Southland Royalty Company has approached this weight of precedent by arguing that none of the cases on this subject matter are relevant to its fact situation. (See: *Brief of Respondents Southland Royalty Company, et al. in Opposition* dated June 3, 1977, page 7 and footnote 18, responding to petitions for a writ of certiorari. The basis for this statement is that Southland Royalty Company never dedicated gas to interstate commerce, nor did Gulf dedicate the Southland Royalty gas to interstate commerce. Southland Royalty Company has consistently argued that their gas is somehow separate and distinct from the gas that has been continuously flowing in interstate commerce for 50 years under the Gulf leases. To follow this argument to its logical conclusion this Court must then accept the premise that under Texas law the leaseholders cannot dedicate rights to property beyond the term of their lease and therefore the Natural Gas Act is not applicable to the subject gas.

This theory contradicts the entire line of case law in the subject area. It has not been suggested that Southland Royalty Company somehow sought a dedication of gas in interstate commerce or that Gulf in Southland Royalty Company's name sought to dedicate Southland Royalty Company's gas in interstate commerce.[12] Rather, the abandonment provision of Section

---

[12]In their briefs in the Court below, Southland Royalty Company, et al. (Southland Brief p. 11), Texaco Inc., and Mobil Oil Corporation (Texaco Brief p. 7) argued that the case of *Mobil*

7(b) attaches to the subject gas by reason of the Natural Gas Act itself. There is no dispute in this case that Gulf had all possessory interests in the gas under the leaseholds including full right of sale. In fact, Gulf not only had the authority under its leases to develop and market the gas interstate but also had the reciprocal duty under the leases to do so, as a gas lease requires the development and marketing of the gas. As a result of its sale of the gas produced for resale in interstate commerce, Gulf dedicated all the natural gas from the acreage covered by the leases to interstate commerce. The certificates of public convenience and necessity issued by the Commission contained no time limitation nor limitation as to the amount of gas under the acreage that could be sold in interstate commerce. In short, the instant fact situation is explicitly covered by *Sunray Mid-Continent Oil Company* and the line of cases that follow it.

Oil Corporation v. Federal Power Commission, 463 F.2d 256 (D.C. Cir. 1971), cert. denied, 406 US 976 (1972) governed the instant fact situation. In the *Mobil* case it was found that the ownership of a royalty interest in gas flowing in interstate commerce did not make the royalty owner subject to the Natural Gas Act. This argument was presented presumably because petitioners in the court below failed to appreciate that the Natural Gas Act applied to the "service" involved in the sale of this flow of natural gas in interstate commerce. They were attempting to bolster their argument that they had not themselves sought to make a dedication of natural gas to interstate commerce. In fact, the *Mobil* case is irrelevant to the instant matter because there is no issue *of a royalty* ownership here. While it is true that *Southland Royalty Company* were royalty owners during Gulf's leasehold, this fact does not constitute an issue in this case. Further, the *Mobil* case does not apply to royalty owners who have since taken actual control of the natural gas and are attempting to remove it from interstate commerce.

Southland Royalty Company contends that the instant situation is different in that, in all other cases construing Section 7(b), the parties seeking to avoid the necessity for an abandonment authorization were either successors in interest to the previous natural gas owners or had themselves dedicated the gas in interstate commerce through since expired contracts. Southland Royalty Company submits that they never were possessed of the gas in question during Gulf's leasehold nor succeeded to Gulf's interests. The fallacy of this argument is that it seeks to make a technically legal distinction while ignoring the purpose of the Natural Gas Act and the abandonment provision therein. While it might be correct that the legal arrangement between the private parties in this case is somewhat different than such arrangements in cases previously before this Court, that fact in itself does not warrant a ruling in favor of Southland Royalty Company. Southland Royalty Company has not explained why, when judged against the language of the Act and the purposes to be served by the Act, their transaction should be freed from the duty imposed by that Act.

A review of the cases interpreting the Natural Gas Act reveals a history of decisions that looked beyond a cursory reading of the language of the Act to seek out the public interest. *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591 (1944) upheld the validity under the Natural Gas Act of a rate order by the Commission reducing rates stating the Commission's ratemaking function involves the

making of pragmatic adjustments. The Court noted that the primary aim of the Natural Gas Act was to protect consumers against exploitation at the hands of natural gas companies. 320 U.S. 591, 610. The respondent in the *Hope Natural Gas Company* case argued among other things that the Natural Gas Act did not grant such broad powers to the Commission.

Phillips Petroleum Company v. Wisconsin, 347 U.S. 672 (1954) ruled that Commission regulation applied to an independent producer of natural gas as being engaged in the sale in interstate commerce of natural gas for resale even though the producer did not engage in the interstate transmission of gas. This Court discussed the legislative history and the Congressional intent to protect the consumer to determine that Section 1(b) of the Natural Gas Act applied to the independent producer.

In *Federal Power Commission v. Transcontinental Gas Pipe Line Corp.,* 365 U.S. 1 (1961) the Commission authority to deny a certificate of public convenience and necessity for a "direct sale" to a public utility was upheld when the reason for the denial was that the gas was to be used to burn under boilers, a use the Commission believed to be inferior. As a direct sale, the transaction involved in that case did not come under the Commission's jurisdiction except for the granting of a certificate authorizing transportation under Section 7. This Court considered the question of whether such a broad policy issue as the end use of the gas was within the language of the

Natural Gas Act. In again analyzing Congressional intent this Court stated: "The Commission is the guardian of the public interest in determining whether certificates of convenience and necessity shall be granted. For the performance of that function the Commission has been entrusted with a wide range of discretionary authority." 365 U.S. 1, 7. Quoting from its ruling in *Panhandle Eastern Pipe Line Co. v. Public Service Commission of Indiana, et al.,* 332 U.S. 507 (1947) the Court reaffirmed its belief that the Congress meant to "create a comprehensive and effective regulatory scheme to protect consumers." 365 U.S. 1, 19.

Federal Power Commission v. Louisiana Power and Light Company, 406 U.S. 621 (1972), upheld the Commission's power to authorize a jurisdictional pipeline's curtailment plan applicable to both its direct sales customers and its resale customers. The direct sales customers objected on the basis that Section 1(b) only applies to sales of gas in interstate commerce for resale and direct sales are specifically exempted. This Court found that Section 1(b) involved three entirely separate regulatory areas: (1) transportation of natural gas in interstate commerce; (2) sales for resale in interstate commerce; (3) natural gas companies engaged in such transportation or sale. 406 U.S. 621, 636. Contrary to what might appear from an initial reading of the subject section, the Court found a Congressional intent to treat each of these as an independent grant of jurisdiction. Therefore, in the *Louisiana Power and Light* case, the

jurisdiction over transportation was not limited by the limits on the jurisdiction over sales. A curtailment plan was found to be within the Commission's jurisdiction over transportation.

California acknowledges that the mere need for federal regulation does not establish Commission jurisdiction if Congress has not granted it. However, we contend that the mere assertion that a particular legal arrangement is not specified on the face of the Natural Gas Act is insufficient as an argument that Southland Royalty Company is free of that Act. Section 7(b) of the Natural Gas Act requires abandonment authorization before gas may be withdrawn from interstate commerce. The ruling of the Court below allowing the exemption of Southland Royalty Company creates just the "attractive gap" in regulation that Congress sought to avoid in seeking to protect the consumer.

It is submitted that the language of the Natural Gas Act taken together with the purposes to be served by that Act lead to the conclusion that Congress intended the instant transaction to be governed by Section 7(b) of the Natural Gas Act.

II. THE PURPOSES TO BE SERVED BY THE NATURAL GAS ACT REQUIRE A REVERSAL OF THE LOWER COURT'S DECISION.

The cases cited in the above section of this brief were not decided solely on legal precedent or a technical reading of a statute. This Court has been very

thorough in seeking the meaning of the Natural Gas Act not only through Congressional intent but also by using a common sense approach of viewing the actual economic and public policy consequences of the particular transactions before the Court. For the Natural Gas Act must be interpreted within the context of the real world events which Congress believed generated a need for regulation. The basic overriding concern throughout the Natural Gas Act and significantly so in Section 7(b) has been the effect a particular action will have on the public interest. In more specific terms, this Court has looked at economic effects, effects on service, the need for comprehensive regulation and the effects avoidance of regulation will have on the regulatory scheme and the public.

Federal Power Commission v. Hope Natural Gas Company, supra, in deciding the scope of the Commission's discretion in carrying out its responsibilities under the Natural Gas Act started with the premise that the primary aim of this legislation was to protect consumers against exploitation at the hands of natural gas companies. 320 U.S. 609, 610. Congress in enacting the Natural Gas Act gave the Commission broad powers of regulation in setting just and reasonable rates and in controlling entrance to and exit from the interstate market under Section 7. 320 U.S. 609, 611. In the *Hope Natural Gas Company* case the Court logically considered the economic restrictions that respondent's arguments would have on the Commission's ability to protect the public from economic exploitation and found that such arguments,

if successful, would contravene the purpose of the Act. This type of analysis was carried forward to the *Catco* case, 360 U.S. 378, 388, in which this Court stated that the purpose of the Natural Gas Act was to underwrite just and reasonable rates to the consumers of natural gas. In fact, the Court in *Catco* began its analysis of petitioners' arguments by first putting in focus the purposes to be served by the Act, then listing the provisions of the Act that carry out those functions and, finally looking at the practical effect that the petitioners' arguments, if successful, would have on the policies to be protected. In this case the Court concluded: "When the proposed price is not in keeping with the public interest . . . the Commission in the exercise of its discretion might attach such conditions as it believes necessary." 360 U.S. 378, 391.

The *Sunray Mid-Continent Oil Company* proceeding brought the application of this approach directly to the consideration of Section 7(b). This Court, looking at the practical consequences of limiting the abandonment provision of the Act, started with the domino effect caused by a producer that could obtain a certificate of public convenience and necessity for a limited period and thereby avoid the need for abandonment authorization. Carrying this chain of events through to the pipeline company serving a community, the Court recognized the economic stranglehold such a situation would create. "And this, though the primary practical problem that led to the passage of the Act was the great economic power of the pipeline com-

panies as compared with that of communities seeking natural gas service. (Citation omitted)." 364 U.S. 137, 143. This Court quickly recognized the danger of narrowly defining the abandonment provision of Section 7(b). "When attached to the leverage of a power to abandon service, at a contract's termination, without contemporaneous Commission approval, this power to exercise contractual control not only over rates but over the mode of this regulation, would be a substantial one indeed."[13] Against this practical backdrop the Court not only stated the principle that the abandonment provision of Section 7(b) must be broadly construed to effectuate the Natural Gas Act but the Court also set forth the more subtle analysis that Section 7(b) contemplates the "service" represented by the movement of gas in interstate commerce not merely the "sale" of gas for resale. In this case where a producer attempted to force the Commission to issue it a limited certificate of public convenience and necessity thereby avoiding the abandonment provision, the Court after reviewing the consequences of this argument on Section 7(b) stated: "The practical reasons behind petitioner's self-abnegating desire to have a limited rather than an unlimited authorization from the Commission are obvious from a study of the Natural Gas Act's provisions. Obvious also is the damaging effect that acceptance of petitioner's central contention would have upon the policies of the Act."[14]

---

[13] *Sunray Mid-Continent Oil Company v. Federal Power Commission, supra,* at 147.

[14] *Sunray Mid-Continent Oil Company v. Federal Power Commission, supra,* at 141.

This Court has continued to maintain a strong support of Section 7(b) based on these public interest considerations and a recognition of the damage that could be done to regulation under the Act if abandonment authorization could be avoided.[15] Even in *Federal Power Commission v. Moss,* 424 U.S. 494 (1976) where the Commission's authority was upheld in issuing pregranted abandonment authorization commensurate with a sales contract in special instances to stimulate domestic exploration and development of natural gas reserves, Chief Justice Burger in a concurring opinion voiced his disapproval of this approach on the above-stated public policy grounds.

> "This factor of unregulated choice by the producer raises the very evils which the Court pointed out in Sunray II, supra: '[E]very independent producer of natural gas . . . [would] be free at a future date, untrammeled by Commission regulation, to reassess whether it desired to continue serving the interstate market.' 364 U.S. at 142, 4 L.Ed. 2d 1623, 80 S.Ct. 1392."[16]

A determination based on the public interest has also been the cornerstone of the resolution of issues in those cases before this Court where the issues were not foreseen when the Natural Gas Act was created. In *United Gas Improvement Company v. Continental Oil Company, et al.,* 381 U.S. 392 (1965), the Commission asserted jurisdiction over, and refused to

[15]See *United Gas Pipe Line Co. v. Federal Power Commission, supra,* at 88, *Sun Oil Company v. Federal Power Commission,* 364 U.S. 170, 175 (1960).

[16]*Federal Power Commission v. Moss, supra,* at 506.

approve the sale of leasehold interests where a natural gas company which owned and operated an interstate pipeline transmission system purchased the leases in a field of proven and substantially developed reserves of gas. The Court upheld the Commission's determination that this was in reality a sale of natural gas for resale in interstate commerce. In making its determination this Court considered the effect on the Natural Gas Act of denying the Commission jurisdiction.

> "Acceptance of any such narrow interpretation would make Phillips [*Phillips Petroleum Co. v. Wisconsin*] a shadow. Its substance lies, instead, in the judgment that '[p]rotection of consumers against exploitation at the hands of natural-gas companies was the primary aim of the Natural Gas Act [citation omitted] . . .'"[17]

In both *Federal Power Commission v. Louisiana Power and Light Company, et al., supra,* and *Federal Power Commission v. Transcontinental Pipe Line Corp., supra,* where the Commission's power to curtail gas deliveries to end uses on broad policy grounds was upheld, this Court based its analysis on the protection of the consumers, citing *Hope Natural Gas Company* and *Sunray Mid-Continent Oil Company.* The Court recognized that Congress meant to create a comprehensive and effective regulatory scheme to protect the consumer interest. 406 U.S. 621, 631. The Commission is required by this Court to look at the

[17]*United Gas Improvement Co. v. Continental Oil Co., supra,* at 402.

backdrop of the practical consequences resulting from its action and the purposes of the Act." That is what it has done in the instant case. Against the singular claim that the particular private legal arrangement entered into by Southland Royalty Company is exempt from Section 7(b) of the Natural Gas Act, the Commission has weighed both the requirement of this Court that it enforce that provision as well as the practical consequences of allowing such an exemption.

For the Commission must consider that such fixed-term leases as are under consideration here could become prevalent as a means to thwart Commission jurisdiction. As is being attempted in this case, future lessors could freely move from the interstate to the intrastate market with the Commission helpless to consider the public interest. Several variations of lease arrangements could be and in fact have been created that reach this result. For example, a producer recently argued before the Commission that a Section 7(b) proceeding was not required where the Commission had issued a certificate for the sale of gas in interstate commerce from certain acreage. The producer had begun production and sales of gas from only a portion of that acreage covered by the certificate, allowing the leases covering the remaining parcels of land in the acreage to lapse. As to the leases which lapsed, it was argued that no abandonment authorization was required even though the certificate embraced the gas associated with these

[18] *Federal Power Commission v. Hunt*, 376 U.S. 515, 525 (1964).

leases. The Commission rejected this argument.[19] In the instant case, the practical consequence of accepting Southland Royalty Company's argument is to place the consideration of the public interest as to abandonment in private hands. The economic effect on the consumers so oft referenced in cases on abandonment authority is especially critical here. Recent energy shortages plus the unregulated nature of the intrastate gas market have created a tremendous disparity between intrastate and interstate gas prices. It is reasonable to assume that natural gas producers will look to all possible means of selling their gas in the intrastate market to the economic and "service" detriment of the consumer. These are the very attacks on the public interest that *Sunray Mid-Continent Oil Company* required the Commission to guard against.

CONCLUSION

The Natural Gas Act, Section 7(b), unequivocally precludes abandonment of a constant flow of natural gas in interstate commerce without Commission authorization. This requirement cannot be circumvented by private agreement. Without this requirement in the Act, there would be no way to protect the consumers against economic exploitation by the

[19] *Northern Natural Gas Co. v. John L. Crawford*, Docket No. CS 71-6 (issued September 29, 1976), appeal docketed *sub nom. Harrison v. Federal Power Commission*, (5th Cir.) No. 76-4318, December 19, 1976.

natural gas producers. Therefore, California prays that the judgment of the United States Court of Appeals for the Fifth Circuit be reversed, and that the orders of the Federal Power Commission involved herein be affirmed.

Respectfully submitted,

JANICE E. KERR,
J. CALVIN SIMPSON,
RANDOLPH W. DEUTSCH,
5066 State Building,
San Francisco, California 94102,
Attorneys for Petitioners the People of the State of California and the Public Utilities Commission of the State of California.

Dated: August 30, 1977.

(Appendix "A" Follows)

APPENDIX A

Appendix A

The Natural Gas Act, 52 Stat. 821-833, as amended, 15 U.S.C. 717-717w, provides in pertinent part:

Section 1(b):

> The provisions of this act shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural-gas companies engaged in such transportation or sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas. [15 U.S.C. 717(b)]

Section 7(b):

> No natural-gas company shall abandon all or any portion of its facilities subject to the jurisdiction of the Commission, or any service rendered by means of such facilities, without the permission and approval of the Commission first had and obtained, after due hearing, and a finding by the Commission that the available supply of natural gas is depleted to the extent that the continuance of service is unwarranted, or that the present or future public convenience or necessity permit such abandonment. [15 U.S.C. 717f(b)]

Section 7(c):

> No natural-gas company or person which will be a natural-gas company upon completion of any proposed construction or extension shall en-

gage in the transportation or sale of natural gas, subject to the jurisdiction of the Commission, or undertake the construction or extension of any facilities therefor, or acquire or operate any such facilities or extensions thereof, unless there is in force with respect to such natural-gas company a certificate of public convenience and necessity issued by the Commission authorizing such acts or operations: *Provided, however,* That if any such natural-gas company or predecessor in interest was bona fide engaged in transportation or sale of natural gas, subject to the jurisdiction of the Commission, on February 7, 1942, over the route or routes or within the area for which application is made and has so operated since that time, the Commission shall issue such certificate without requiring further proof that public convenience and necessity will be served by such operation, and without further proceedings, if application for such certificate is made to the Commission within ninety days after February 7, 1942. Pending the determination of any such application, the continuance of such operation shall be lawful.

In all other cases the Commission shall set the matter for hearing and shall give such reasonable notice of the hearing thereon to all interested persons as in its judgment may be necessary under rules and regulations to be prescribed by the Commission; and the application shall be decided in accordance with the procedure provided in subsection (e) of this section and such certificate shall be issued or denied accordingly: *Provided, however,* That the Commission may issue a temporary certificate in cases of emergency, to assure maintenance of adequate service or to serve particular customers, without notice or hearing, pending the determination of an application for a certificate, and may by regulation exempt from the requirements of this section temporary acts or operations for which the issuance of a certificate will not be required in the public interest. [15 U.S.C. 717f(c)]

Section 7(e):

Except in the cases governed by the provisos contained in subsection (c) of this section, a certificate shall be issued to any qualified applicant therefor, authorizing the whole or any part of the operation, sale, service, construction, extension, or acquisition covered by the application, if it is found that the applicant is able and willing properly to do the acts and to perform the service proposed and to conform to the provisions of the Act and the requirements, rules, and regulations of the Commission thereunder, and that the proposed service, sale, operation, construction, extension, or acquisition, to the extent authorized by the certificate, is or will be required by the present or future public convenience and necessity; otherwise such application shall be denied. The Commission shall have the power to attach to the issuance of the certificate and to the exercise of the rights granted thereunder such reasonable terms and conditions as the public convenience and necessity may require. [15 U.S.C. 717f(e)]